A Note to Help you Outline Your strategy

This note was sent to you in the debrief for practice round 3. It is pertinent to revisit it now.

Teams may find it useful to go through the 6 strategies given on the CAPSIM (Help>Online Guide>Six Basic Strategies). It is *not* necessary to adopt one of these six strategies. They are simply a broad guide that illustrate that strategic management makes sound business sense. A well thought through and cogent strategy, well executed will invariably come a winner.

Outline Your Strategy: A Note

At the beginning of the simulation, your team faces an unusual business situation – all companies and products are identical to each other. In the real world this situation rarely if ever occurs. The closest analogue might be a highly regulated industry.

Looking into the future, the simulated industry will rapidly differentiate and evolve. As in the real world, **nothing you can do will stop it.** Given time, the industry will evolve into a state where competitors occupy defendable strategic positions. **There are two important questions. “How long will the process take?” “Will two or more competitors attempt to occupy the same position?”**

Let’s use an analogy. Picture a flat landscape. Now imagine several hills placed on the landscape. Each of the hills represents a strategy. Your success depends upon how quickly you can identify a hill, and how high you can climb it. Your hope is that you will choose a hill that nobody else picks, and that you can defend it against competitors. Complicating this is the fact that some hills are more attractive than others. Further, the more companies trying to climb a particular hill, the more difficult it is for each of them to successfully climb it.

Are there methods and techniques that will help you identify and select these strategic hills? Yes, the general topic is widely discussed. Let’s look at one of the most commonly referenced, Michael Porter’s “Generic Strategies”. Read the description offered on The QuickMBA website at http://www.quickmba.com/strategy/generic.shtml (A quick search of www.google.com for “Porter Generic Strategies” will turn up hundreds of alternate references. The QuickMBA’s one page summary is an excellent overview of the topic, but feel free to examine others.)

Next, review Chapter 10 of the Student Guide, "6 Basic Strategies."

With this as background, select or develop a strategy you would like your team to pursue. Prepare and post an argument for your strategy. **The argument should**

address these issues:

1. **Segments. Which segments matter to you? How much share of those segments must you achieve to be an "average competitor" in the overall industry?** For example, if you choose to play only in Traditional and Low End, you would have to command a higher share of those segments to achieve "average industry sales".

2**. Profit potential**.

3. **The speed at which you can create a defendable position**. For example, new products typically take two years to bring to market. Significant productivity improvements could take several years.

4**. Priorities**. Which products are most important to you? Which are least important?

<u>Competitive Advantage and Core Competence: A Note</u>

Let us examine the capabilities your company needs to develop to deliver its strategy. We assume that your team is about to have a meeting to set long range priorities around performance capabilities. This note is pre-work for that meeting.

At this point you have a vision, and you have a strategic direction. For example, you might be saying, "We plan to be a high technology company. We will concentrate our resources upon the High Tech segment. We will compete based upon differentiation." Or you might have decided to be in every segment and compete on price, or any of a dozen other combinations of vision and strategy.

But what capabilities do you need to develop to execute your strategy? For example, it is one thing to say, "We will compete on price", and another to build a company that can effectively compete on price and still produce a solid return for stakeholders.

Let's relate two popular ideas, "Core Competence" and "Competitive Advantage", to your situation. You will find dozens of references to "Core Competence" (C.K. Prahalad and Gary Hamel) and "Competitive Advantage" (Michael Porter) on the Internet. (For example, try the QuickMBA. http://www.quickmba.com/strategy/core-competencies/ and http://www.quickmba.com/strategy/competitive-advantage/.)

You could develop competencies in awareness, accessibility, product redesign, product invention, automation, plant utilization, human resources, cash flow management, and forecasting. All of these competencies take several years to develop.

You would use these competencies to develop competitive advantages. For example, competencies in automation and human resources could lead to a competitive advantage in cost leadership. Competencies in awareness, accessibility, and design could lead to a competitive advantage built upon differentiation.

With this as background, think about **three key questions**:

1. **What are the top three competencies you believe necessary to execute your vision and strategy?**

2. **What decisions do you need to make to develop these competencies?**

3. **How will they produce competitive advantage?**

A PERTINENT NOTE: Retained Earnings

A query raised by a participant recently was:

"I have $X million in retained earnings, but I'm unable to use it to retire part of my debt. Why do I have to borrow when I have such large retained earnings? "

It's good that this question was raised. A number of senior execs in industry with fancy MBAs also falter fundamentally here. Countless MBAs across the world can get top marks in accounting and finance courses without getting this foundational truth right.

This basic funda, if not cleared now, can stick with the best of us throughout a lifetime. Capstone will help clear numerous fundas across functions. Pay attention to the basic accounting equation above.

Remember Assets = Liabilities + Contributed Capital + Retained earnings.

Quite simply, all your retained earnings are **<u>not</u>** available in the form of cash. Your firm retained some of the earnings, but it locked up in assets other than cash as your firm made investments for growth. Look at you balance sheet and compare assets with liabilities.

Why did the firm retain some part of the earnings in the first place, rather than give it back to the stockholders? Answer: to invest in growth opportunities. Hence the firm **invested part or whole of** that cash (from retained earnings) in growth opportunities - e.g enhancing plant size, more inventory build up , promo etc etc. (keeping it in cash in the current account at the bank would really not constitute a growth investment).

So in the accounting equation above, as you earn more and retain more earnings and then make growth investments for your firm, more of your assets are financed by the retained earnings. You create more assets from those retained earnings. Assets are your use of funds. The right side of the equation if the source of those funds!

Remember to look at your **proforma** balance sheet and the finance sheet on Capstone - observe the capital structure of the firm. Based on your sales forecasts and costs it tells you how much cash you will have. Remember, it is a projection and may not come true.

It's not for nothing that they say "cash is king". Too little cash can lead to a liquidity crisis during the ups and downs of business. Too much cash lying idle indicates that the financial managers in the firm have run out of options to use the funds (and may need to be replaced with others with more initiative).

You are the CEO, you have to make the choice.